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In the

Supreme Court of the United States

OCTOBER TERM, 1945

No. 504

POND FORK OIL & GAS COMPANY, *Petitioner,*

versus

ALBERT H. COLE, H. LANGDON LAWS and CHARLES H. STEPHENS, JR., Trustees of the Cole & Crane Real Estate Trust, *Respondents.*

BRIEF IN OPPOSITION TO GRANTING WRIT OF CERTIORARI TO THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

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SUBJECT INDEX

	Page
STATEMENT OF THE CASE	1-6
ARGUMENT	7-13
CONCLUSION	14

TABLE OF CASES AND AUTHORITIES CITED

Acts 1939 Legislature of West Virginia, Ch. 127 ..... 2, 3, 5, 11, 13

Barwise v. Sheppard, 299 U. S. 33 13

Code of West Virginia, Ch. 11, Art. 13 ..... 3, 4, 5, 7, 8, 9, 12

Code of West Virginia, Ch. 11, Art. 13, Sec. 2-a 2, 3, 4, 9, 10, 12

Code of West Virginia, Ch. 11, Art. 13, Sec. 3-a 2

Code of West Virginia, Ch. 11, Art. 13, Sec. 2-j 2, 3

Constitution of the United States, Art. I, Sec. 10 ..... 2, 6

Constitution of West Virginia, Art. III, Sec. 4 ..... 2, 6

Constitution of West Virginia, Art. VI, Sec. 30 ..... 2, 5, 6, 7, 10, 13

Constitution of West Virginia, Art. VIII, Sec. 5 10

Constitution of West Virginia, Art. X, Sec. 1 3

Freidrich v. Wright, 386 Ill. 229, 53 N. E. 2d 974 ..... 8, 12

Kanawha Valley Bank v. United Fuel Gas Company, 121 W. Va. 96 ..... 3, 4, 8, 12

Lynch v. New York ex rel. Pierson, 293 U. S. 52 7

Norum v. Oil Co., 83 Mont. 853, 272 P. 534 ..... 4, 8, 12

Ohio Oil Co. v. Wright, 386 Ill. 206, 53 N. E. 2d 966 ..... 8, 12

Roby v. Sheppard, 42 W. Va. 286 5

Willoughby on the Constitution of the United States, 2d. Ed., Vol. 2, p. 1300 12

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STATEMENT OF THE CASE

By a written lease made March 18, 1924, respondents leased land lying in West Virginia to one C. A. Croft for oil and gas purposes in consideration, inter alia, of Croft's covenant to pay respondents one-eighth of the proceeds from the sale of the natural gas produced from the leased land, and in no case less than one cent for each one thousand feet of gas produced. Prior to June 1, 1939, petitioner, through mesne assignments, became the owner of Croft's rights and assumed all of his obligations under the lease. A number of producing gas wells were drilled

on the leased land by petitioner or its predecessor in title. Until June 1, 1943, they paid the full amount of the rental agreed upon, and thereby complied fully with said covenant. However, petitioner failed and refused to pay a substantial part of the agreed rental which accrued for the months of June, July and August, 1943, claiming the right to withhold such payment because the sum withheld equalled one-eighth of certain occupation taxes which were paid by petitioner, and which were imposed upon petitioner by Sections 2-a and 3-a, Article 13, Chapter 11 of the Code of West Virginia, for the privilege of engaging in the business of producing natural gas. Respondents brought suit to recover the unpaid rentals and petitioner demurred to respondent's complaint and set up as its authority for paying less than the rentals agreed upon in the lease, Chapter 127 of the Acts of the 1939 Legislature of West Virginia (now Section 2-j, Article 13, Chapter 11, Code of West Virginia). The validity of said Section 2-j was thus put in issue. The trial court upheld the act, but on its own motion certified to the Supreme Court of Appeals of West Virginia the question of whether or not its ruling was correct. The Supreme Court of Appeals of West Virginia decided that the act was unconstitutional and void because it was in violation of Section 30, Article VI of the Constitution of West Virginia, and also because it was in violation of Section 4, Article III of the Constitution of West Virginia and Section 10, Article I of the Constitution of the United States.

Respondent's complaint (called a "Notice of Motion for Judgment" under the West Virginia statute) will be found on pages 3 to 12 of the record. The lease is set forth in the complaint, and will be found on pages 4 to 8 of the record. Petitioner's demurrer appears at pages 15 to 18, and the above mentioned statutes, which are copied into the opinion of the Supreme Court of Appeals of West Virginia, will be found on pages 24 to 26 of the record.

Prior to the passage of the questioned act (Chapter 127 of the Acts of the 1939 Legislature of West Virginia, now Section 2-j, Article 13, Chapter 11, Code of West Virginia), Article 13 of Chapter 11 of the Code of West Virginia imposed taxes upon certain persons for the privilege of engaging in certain occupations or businesses, such as the business of manufacturing, the business of selling tangible property, the business of operating a utility, the business of contracting, the business of making industrial loans, the business of operating a theater, the business of collecting incomes, the business of producing natural gas for sale, etc. The language of the statute with respect to the privilege of engaging in the last named occupation or business being—

> "There is hereby levied and shall be collected annual privilege taxes * * upon every person engaging or continuing within this state in the business of producing for sale, profit or commercial use any * * natural gas * *." (R. 24)

This type of taxation was first adopted in West Virginia in 1921 under the authority of Section 1, Article X of the Constitution of West Virginia, which permitted the Legislature to tax privileges (R. 32). At that time, the Legislature discarded the idea of a production tax, i. e., a tax based on the ownership of the thing produced, in favor of a tax on the privilege of engaging in certain occupations some of which result in the production of commodities and others do not; and the Legislature has adhered to that choice (R. 32).

In 1938 a West Virginia oil and gas operator undertook to shift to its lessor part of the tax imposed upon it for the privilege of engaging in the oil and gas business by said Section 2-a. The question of its right to do so reached the Supreme Court of Appeals of West Virginia early in 1939 in the case of *Kanawha Valley Bank v. United Fuel Gas Company*, 121 W. Va. 96. That Court held

that the gas operator had no right to make any deduction from the rental or royalty provided for in the lease because of taxes paid by the operator for the privilege of engaging in that occupation. The necessary effect of the West Virginia decision was that the land owner (the lessor) was not engaged in a joint enterprise with the lessee in producing natural gas; nor was the land owner in any sense engaged in that occupation. The Court cited *Norum v. Oil Co.*, 83 Mont. 353, 272 P. 534, with approval. In that case the Montana Court described a similar tax as—

> " * * An occupation license tax, as distinguished from a property tax, and applies only to persons *engaged* in the *business* of producing oil. The owner of the land, as such, is not engaged in the *business* within the purview of the act. He merely grants a right to the operator to engage in such business upon his land. Under the lease, the well is drilled and the oil produced therefrom by the operator, not by the land owner, and the well is subject to the exclusive control of the lessee so long as he performs all of the conditions of the lease." (Emphasis by the Court.)

The West Virginia Court again cited the *Norum* case with approval in the case at bar.

Not long after the *Kanawha Valley Bank* decision, the West Virginia Legislature passed the act in question as an amendment to said Article 13, Chapter 11 of the Code of West Virginia. This amendment undertakes to authorize persons engaging in the occupation of producing natural gas to deduct from royalty owing by them to their lessors that portion of the taxes imposed upon them by said Section 2-a for the privilege of engaging in that occupation, and paid by them, which said royalty bears to the entire production from the leased land. It then provides " * * There is hereby levied upon such *royalty interest* such proportionate part of the tax imposed (upon the lessee operator) by said Section 2-a." (The words in parentheses and the emphasis supplied by us).

This is the act (R. 25, 26) relied upon by petitioner as its authority for withholding part of the rental or royalty which it has agreed in said lease to pay to respondents.

The validity of this act was attacked by respondents in the West Virginia Court on several grounds. One was that the act is bad because it is in violation of Section 30, Article VI of the West Virginia Constitution, which provides in part—"No act hereafter passed, shall embrace more than one object, and that shall be expressed in the title." Under this constitutional provision an act amending a former act need not repeat the title but may refer to the chapter, article and section of the Code where the former act is to be found. But the amendment must be germane to the original act for, " * * if foreign to the prior legislation, it would violate that clause of the Constitution saying that an act shall have but one object." *(Roby v. Sheppard*, 42 W. Va. 286, see also R. 32, 33).

In the case at bar the Supreme Court of Appeals of West Virginia decided that the 1939 act was in violation of the above mentioned section of the West Virginia Constitution because the original taxing statute, which is now Article 13, Chapter 11 of the West Virginia Code, and which the 1939 act purported to amend, created a system of taxation whereby taxes are imposed for the privilege of engaging in certain occupations, (R. 32), whereas the 1939 act (if its real intent was to levy any tax at all) undertook to levy a tax "upon such royalty interest" which is a tax upon property rather than upon the privilege of engaging in an occupation. Such a tax is not germane to a privilege tax and may not be included in the same statute or an amendment thereto. Also the title to the act fails to express properly this new object. This disposed of the case and the opinion need not have gone farther.

That this is the principal basis of the decision of the West Virginia Court appears, not only from the opinion

itself, which will be hereinafter discussed in the argument, but from the first two points in the syllabus, written by the Court, in compliance with a requirement of the Constitution of that State. This syllabus is the law of the case. It contains three points and the first two show beyond question that the primary reason for the decision is the violation of Section 30 of Article VI of the West Virginia Constitution.

Another ground upon which respondents attacked the validity of said act was that it impairs the obligation of the contract between respondents and petitioner, and thereby violates the provisions of Section 4 of Article III of the West Virginia Constitution, which provides in part "No * * law impairing the obligation of a contract * * shall be passed," and also Section 10, Article I of the Constitution of the United States. The West Virginia Court having concluded that the act violates Section 30 of Article VI of the West Virginia Constitution because it attempts to combine in one statute the imposition of two separate and distinct, and wholly unrelated, kinds of taxes, went on to find that the statute was nothing more than a barefaced attempt to change the terms of the contract beween the petitioner and respondents and, therefore, was in violation of the contract clauses of the West Virginia Constitution, and of the United States Constitution. This conclusion is stated in the third and last point of the Court's syllabus.

ARGUMENT

Where the judgment of the state court rests on two grounds, one involving a federal question and the other not, and the latter, independent of the former, is sufficient to sustain the judgment, the Supreme Court will not take jurisdiction.

This Court has said in *Lynch v. New York ex rel. Pierson*, 293 U. S. 52:

> "It is essential to the jurisdiction of this Court in reviewing a decision of a court of a State that it must appear affirmatively from the record, not only that a federal question was presented for decision to the highest court of the State having jurisdiction but that its decision of the federal question was necessary to the determination of the cause, and that it was actually decided or that the judgment as rendered could not have been given without deciding it. (Citing cases) Where the judgment of the state court rests on two grounds, one involving a federal question and the other not, or if it does not appear upon which of two grounds the judgment was based, and the ground independent of a federal question is sufficient in itself to sustain it, this Court will not take jurisdiction." (Citing cases)

An examination of the opinion of the West Virginia Court discloses that the non-federal ground of the decision is not only sufficient to sustain the judgment, independent of the federal question, but that the non-federal ground, namely the violation of Section 30, Article VI of the West Virginia Constitution, is the primary basis for the decision.

The opinion points out that Article 13, Chapter 11 of the West Virginia Code imposes a tax upon the privilege of engaging in certain occupations or businesses, and that " * * beginning in 1921, when the system of indirect taxation was first adopted in this state, the idea of a produc-

tion tax on natural resources was discarded, * * . Certain it is that in our system of indirect taxation we have taken the safe and sure way of taxing privileges as expressly authorized by the Constitution, instead of embarking on a system which might give rise to certain questions concerning equality, uniformity and questions of like nature." (R. 32) "We have no production tax. Our legislature has studiously avoided imposing a production tax, and has resorted to the imposition of a privilege tax, whereby persons, firms and corporations are classified according to the business in which they are engaged, and a tax collected from the gross proceeds of their business rather than upon any product which they may produce from the earth or manufacture or process." (R. 35)

In other words said Article 13 imposes an excise tax upon the privilege of engaging in certain occupations or businesses. It does not impose a tax upon the thing produced or a tax based upon the ownership of the thing produced. Most of the occupations taxed by that article do not even result in the production of a commodity; for example, making industrial loans, contracting, operating a theatre, selling tangible property, collecting incomes, etc. This then is the theory of taxation carried out in said Article 13.

The Court points out that the farmer or other person who leases his land to an oil and gas operator whereby the latter acquires the right to explore for oil and gas and to remove it, if found, from the land, does not thereby engage in the business or occupation of the oil and gas operator. *(Kanawha Valley Bank v. United Fuel Gas Company, supra; Norum v. Oil Co., supra; Freidrich v. Wright*, 386 Ill. 229, 53 N. E. 2d 974; *Ohio Oil Co. v. Wright*, 386 Ill. 206, 53 N. E. 2d 966; see also page 3, *supra.)* Generally speaking, the oil and gas lessor " * * parts with every vestige of control over the production of oil and gas in the property he leases." (R. 28)

Thus it may be inferred that the legislature, even if it attempted to do so, could not convert a lessor into an oil and gas operator, contrary to the fact, and make him pay taxes for the privilege of engaging in a business in which he does not engage, although it may, of course, tax him for engaging in any business in which he does engage, such as leasing land, receiving income, etc. "The legislature does not have the power to declare that not to be a fact which everyone knows is a fact; and * * by the same reasoning, cannot legislate that to be a fact which everyone knows is not a fact." (R. 28)

But this point does not appear to be necessary to the decision of the case because the Court rightly found that the only taxing provision in the questioned act constituted an attempt by the legislature "to lay a tax on the lessor's interest in accrued royalties * * * " which are personal property, and if personal property, can only be taxed in accordance with the provisions of law covering other classes of personal property. (R. 29) The 1939 Act provides that the oil and gas operator, having paid the tax imposed upon him (but not upon the lessor) by said Section 2-a for the privilege of engaging in the business of producing and selling oil and gas, may deduct part of what he has paid from rental which he has contracted to pay his lessor. The Act then provides " * * * and there is hereby levied upon such royalty interest * * such proportionate part of the tax imposed (upon the oil and gas operator, not the lessor) by said Section Two-a." (The parenthetical phrase inserted by us). The Court held: "What the Act attempts is to levy a tax upon accrued royalty." (R. 32) "The legislation under attack in this case attempts to impose a direct tax upon royalty." (R. 33) The court posed the question: "How in the guise of an amendment to Article 13 of Chapter 11 of the Code can a tax be imposed upon accrued royalty?" (R. 32) And the Court said, "The taxation of oil and gas is entirely outside the purpose of Article 13, the law being amended. In our opinion the ef-

fort to impose a tax upon royalty interest was futile and no tax was imposed." The Court said that this disposed of the contention that the enactment of the tax is covered by the title to the act. (R. 33) The Court concluded: "We hold, therefore, that the imposition of a tax upon royalty was invalid and of no effect * * " because the act undertook to levy a tax upon personal property rather than upon the privilege of engaging in an occupation and, therefore, ran counter to the provisions of Section 30, Article VI of the West Virginia Constitution. And at another point, the Court made the following statement of the grounds upon which its judgment is based—"We hold that the Legislature had no constitutional right to make such an enactment for two reasons: First: There is nothing whatever in the title of the bill to give any notice or intimation that the purpose thereof was to make an apportionment of the tax accruing under Section 2-a * * * ." (R. 31)

Finally, the Constitution of West Virginia (Section 5, Article VIII) requires the Supreme Court of Appeals of that State to state the reasons for its decisions concisely in writing and to prepare "* * * a syllabus of the points adjudicated, in each case concurred in by three of the judges thereof, which shall be prefixed to the published report of the case." *In West Virginia this syllabus is the law of the case.* In compliance with the Constitution, the West Virginia Court wrote a syllabus in the case at bar containing three points. The first two are as follows:

"Syllabus by the Court

"1. Where a statute is sought to be amended by the Legislature, and the title to the act refers to the statute being amended by chapter, article and section without further reference to the purposes thereof, the enactment must be germane to the purposes of the original act, and where it goes beyond that purpose is invalid under Sec-

tion 30, Article VI of the Constitution of this State, requiring the object of the act to be stated in the title thereof.

"2. A tax on royalty accruing from an oil and gas lease may not be constitutionally laid by an act purporting to amend a statute imposing a tax on the privilege of engaging in certain businesses and occupations, because not germane thereto." (R. 21)

This should be an end of the matter, but we feel justified in commenting briefly on certain statements made by counsel for petitioner in their brief. They say that the decision of the West Virginia Court is based upon "* * * the one proposition that when the Legislature classified these particular businesses for the purpose of taxation it had exhausted its power in that regard and could not thereafter change the classification." The substance of this statement is repeated throughout the brief. It misses the mark completely. The West Virginia Court held nothing of the kind. It held that the 1939 amendment does *not* change the classification of the lessor, (R. bottom p. 28) but attempts to assess part of the tax imposed upon the lessee for the privilege of engaging in the lessee's occupation upon personal property owned by the lessor, i. e. "such royalty interest." Passing by the question of whether or not this could be done by proper legislation, the Court found that it could not be done by an amendment to the West Virginia statute imposing taxes for the privilege of engaging in certain occupations because not germane thereto and hence in violation of the West Virginia Constitution.

Counsel for petitioner also say that the act in question imposes "a tax on the production of natural gas on the parties who receive that production." Both occupation taxes and production taxes are excise taxes, but the former are based solely upon the activity of the person taxed, whereas the latter has no relation to activity or

occupation; it is based solely upon ownership of the thing produced. Obviously the two taxes are fundamentally different in character and could not be combined in one act under the West Virginia Constitution. If counsel intend to say that the supposed tax is on the gas produced, or on "such royalty interest," as the act provides, obviously the provision cannot stand as an amendment to Article 13. If they intend to say that the amendment was intended to reclassify the lessor and make him an oil and gas operator, and thereby tax him under Section 2-a, they run counter to the plain language of the act itself. If that had been the intention of the Legislature it could easily have said so, but the language of the act cannot be read so as to justify that conclusion. It simply does not so provide. It makes no such statement, but on the contrary undertakes to levy a part of lessee's occupation tax "upon such royalty interest." We think the legislative intent must be gotten from the wording of the act alone, and not from something not appearing in it. We think what the legislature did, rather than what counsel thinks it might have done, or could have done, quite properly guided the Court in the construction of this statute. Obviously the West Virginia Court could not, with justification, have reached any other conclusion than the one it did reach. Its construction of the West Virginia statute, with certain limitations, is binding upon all other courts *(Willoughby on the Constitution of the United States*, 2nd Ed., Volume 2, page 1300, and cases cited).

Counsel assert, as if it were an undisputed fact, that —"Petitioner and respondents were engaged in the joint enterprise of producing the natural gas from respondents' property * * . " This statement is not correct. Petitioner was engaged in the business of producing natural gas, but respondents were not. *(See Kanawha Valley Bank v. United Fuel Gas Company, supra; Norum v. Oil Co., supra; Freidrich v. Wright, supra; Ohio Oil Company v. Wright, supra;* and pages 3 and 8 above.)

In discussing the case of *Barwise v. Sheppard*, 299 U. S. 33, counsel erroneously assume that the West Virginia Legislature undertook in the 1939 act to "reclassify" lessors, and they say that the West Virginia Court decided that the Legislature had no right to do so. We have already demonstrated, we think, that the act attempts no change in the classification of lessor, and that the West Virginia Court made no such decision.

No question similar to the one arising under Section 30, Article VI of the West Virginia Constitution arose in the *Barwise* case. It may be noted too that the Texas statute which was before the Court in that case levied a tax based upon the ownership of the oil produced; the statute was not concerned with the activity or occupation of anyone; ownership of the oil alone fixed the tax. It was called a production tax. But by whatever name it may be called, it is not the same tax, nor the same type of tax, as a tax imposed upon the privilege of engaging in certain occupations. The tax was "* * charged ratably against all who have an interest in the oil produced." (See 229 U. S. at page 37; see also R. 35). In the case at bar the West Virginia Court simply held, among other things, that under the Constitution of that State these two types of taxes may not be combined in the same act. When the title of an act states its object to be the imposition of taxes for the privilege of engaging in certain occupations and businesses, that act may not impose taxes on property, or taxes based upon the ownership of property. Obviously that Court did not hold that taxes on property, or based on the ownership of property, may not be imposed by proper legislation which meets the requirements of the Constitution of that State. Certainly all this is a matter for the State of West Virginia. It is not a federal question.

CONCLUSION

We think it clearly appears from the record in this case that the decision of the State Court rests primarily upon the non-federal ground that the 1939 amendment violates that part of the West Virginia Constitution which requires the object of each legislative act to be expressed in the title to the act, and which forbids the inclusion of more than one object in a single act. At least this ground is sufficient to sustain the judgment independent of any question as to the impairment of the contract. Furthermore we are confident that the Court's decision that the contract clauses of the state and federal constitutions were violated is clearly right. We believe it is plain that the act is not a bona fide taxing statute, and that it actually accomplishes nothing, except to benefit the oil and gas operator at the expense of his lessor. But we have not argued that question, feeling confident, as we do, that the decision rests primarily upon non-federal grounds, which alone are entirely sufficient to sustain it. It seems obvious that none of the grounds referred to in Section 5 of Rule 38 of this Court nor in the pertinent federal statute are present here.

It is, therefore, respectfully urged that the petition for a writ of certiorari in this case should be denied.

Respectfully submitted,

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ROLLA D. CAMPBELL,
Of Counsel for Respondents.

Huntington, West Virginia
October 18, 1945.